COMPREHENSIVE ELECTRICITY COMPETITION PLAN

INTRODUCTION

Economic forces are forging a new era in electricity policy, where electricity prices will be determined primarily by the market rather than by regulation. Under this new system, often called "retail choice," consumers are allowed to choose their electricity supplier much like the choice of long distance telephone service that has existed for over a decade. Electricity policy is moving in this direction because subjecting utilities to competition will lead to increased efficiency in the industry and thus benefit the economy and the environment.

The importance of this policy change cannot be overstated. The electricity sector is our nation's most capital intensive industry, holding assets with a book value in 1994 of close to $700 billion. It had total sales of $212 billion in 1996, larger than the telecommunications industry. The industry also has a significant impact on the environment.

In the past, electricity customers did not have the ability to choose their supplier. Instead, under State law, utilities generally were monopolies with both a right and responsibility to serve all consumers in a particular area. The State permitted the utility to charge customers a regulated rate for electric power based on the cost of producing such power plus a "rate of return" on investment.

In general, the electric monopoly system has provided reliable power to electric consumers in the United States. However, a monopoly system has a fundamental weakness: it does not provide incentives to be cost-efficient because a monopoly supplier does not have to compete and essentially has a guarantee that its costs will be recovered.

Under electricity restructuring, competition will replace regulation as the primary mechanism to setting electricity generation prices. Utilities would be required to open up their distribution and transmission wires to all qualified sellers. The transmission and distribution of electricity would continue to be regulated because they will remain monopolies for the foreseeable future. The system would be restructured, not completely deregulated.

THE NEED FOR FEDERAL ACTION

We respect the actions of those States which are in the process of implementing retail competition, and seek to build on, rather than disrupt, those efforts. Nevertheless, effective retail competition cannot happen without federal legislation. First, based on the laws of physics, electrons do not respect State borders. Accordingly, as States remove the constraints of monopoly franchise territories, electricity markets will naturally become more regionalized. Only federal legislation can adequately address the needs of these regional markets.

The electric industry is also hampered by statutes which inhibit the development of competitive markets. The entire federal electricity law framework dates from the New Deal and is premised upon State-regulated monopolies rather than regional competitive markets. Federal law must be updated so that it stimulates, rather than stifles, competition.

Finally, the States alone cannot obtain the full economic and environmental benefits of competition for American consumers. Without comprehensive Federal electricity restructuring legislation, neither State nor federal regulators will have the necessary tools to ensure that regional electricity

markets are truly competitive and operate as efficiently as possible. Moreover, there will be no assurances that support for renewable technologies and other important public purpose programs will continue absent a federal program. Without such tools, electricity prices will likely be higher and the environmental gains which we expect under the Administration's plan will not be fully realized.

BENEFITS OF THE ADMINISTRATION'S COMPETITION PLAN

The Comprehensive Electricity Competition Plan embodies the overall agenda of the Clinton Administration to expand the economy and improve the environment. We believe that a more competitive electricity industry will provide immense benefits to individual American consumers as well as being an overall boon to our economy. It will result in lower prices, a cleaner environment, greater innovation and new services, a more reliable power supply grid, and save the government money.

The Department of Energy estimates that retail competition will save consumers at least $20 billion a year on their electricity bills. This translates into direct savings to the typical family of four of $104 per year. Indirect savings, which would arise from the lower costs of other goods and services in a competitive market, are $128 per year for a typical family of four. Thus, total projected savings for such a family are $232 a year.

Competition will also spark innovation in the American economy, creating new industries, jobs, products and services just as telecommunications reform spawned cellular phones and other new technologies. This will further strengthen our nation's position as the most vibrant and dynamic economy in the world.

Major benefits will accrue to the federal, State and local governments through lower electricity prices. Total government spending on electricity was $19.5 billion in 1995. With competition, these costs are likely to decline by at least 10%, a savings of close to $2 billion year. This restructuring dividend will help governments maintain balanced budgets into the future while meeting critical public needs.

Restructuring will also produce significant environmental benefits through both market mechanisms and policies that promote investment in energy efficiency and renewable energy. Competitive forces will create a efficient, leaner and cleaner industry. For, example, we estimate that our Competition Plan will reduce greenhouse gas emissions by roughly 25 to 40 million metric tons in 2010. A generator that wrings as much energy as it can from every unit of fuel will be rewarded by the market. Today, a monopoly supplier recovers its costs regardless of whether it uses its power resources efficiently. Competition also provides opportunities for consumers to vote with their wallets for green power and facilitates the marketing of energy efficiency services along with electricity.

Restructuring also makes possible the introduction of new policy mechanisms such as the renewable portfolio standard and enhanced public benefit funding, which will guarantee substantial environmental benefits notwithstanding market outcomes. We believe that the environmental benefits from the Administration's restructuring plan, which includes the renewable portfolio standard and the public benefit fund, will outweigh any negative effects associated with the demand increasing effects of lower prices or other factors.

The Administration's specifications for electricity competition legislation, outlined below, reflect the need for the simultaneous calibration of many elements in an interconnected statutory framework in order to achieve the desired bottom line: achieving the economic benefits of competition in a manner that is fair to all Americans and improves the environmental performance of the electricity industry.

Our restructuring proposal is best understood in terms of five main objectives: (1) encouraging States to implement retail competition; (2) protecting consumers by facilitating competitive markets; (3) assuring access to and reliability of the transmission system; (4) promoting and preserving public benefits; and (5) amending existing federal statutes to clarify federal and state authority The discussion below follows this structure.

I. ENCOURAGING STATES TO IMPLEMENT RETAIL COMPETITION

Ten states have enacted legislation implementing retail competition. Nevertheless, in most of the country, electric utilities remain monopolies. We anticipate that most States will recognize the benefits of retail competition, and will implement competition on their own initiative. Nevertheless, the policy of the Administration is to encourage all States to embrace the benefits of retail competition.

A. Retail Competition- Flexible Mandate

Proposal: *Support customer choice through a flexible mandate that would require each utility to permit all of its retail customers to purchase power from the supplier of their choice by January 1, 2003, but would permit States or non-regulated utilities to opt out of the competition mandate if they find, on the basis of a public proceeding, that consumers in the State would be better served by an alternative policy such as a State-crafted retail competition plan or the current monopoly system.*

The Administration believes that federal legislation with a flexible retail competition mandate is the best means to obtain the economic benefits of competition while ensuring that States have the opportunity to tailor their utility systems to meet their unique needs. In our view, this approach strikes the proper balance between the need for federal policy to support competition and the tradition of State determination of retail electricity policy. It also addresses the concerns of some low-cost States that a one-size-fits-all approach to retail competition could lead to increased costs in their States. Finally, the flexible mandate builds on State-restructuring plans that have been enacted to date, rather than disrupting them.

The flexible mandate avoids the constitutional questions that have arisen concerning other retail choice proposals, because it does not require that States administer a federal law. Instead, States have the ability to opt out of retail competition. See Printz v. United States, 117 S.CT. 2365 (1997).

B. Stranded Cost Principle

Proposal: *The Administration endorses the principle that utilities should be able to recover prudently incurred, legitimate and verifiable retail stranded costs that cannot be reasonably mitigated. States would continue to determine recovery of investments, including stranded cost recovery, under State law. This policy should also encourage the use of competitively neutral mechanisms that minimize to the*

maximum extent possible any effect of stranded cost recovery on the choice of supplier or product offering by purchasers of electricity. FERC would have "backup" authority to establish a stranded cost recovery mechanism if a State lacks such authority.

Many industry observers expect that lower prices resulting from the pressure of competition will eliminate or sharply reduce the ability of some utilities to recover their past investments. The inability to recover such past investments results in "stranded costs." Put simply, the implementation of a stranded cost policy requires a determination of who is responsible for paying the difference between the cost of production from power plants that were built when costs were high and today's lower prices -- utility shareholders, ratepayers, or both. But these are not "new" costs. Customers are paying them today. However, they must be addressed as part of the transition to competition or numerous utilities could be bankrupted.

The Administration endorses the principle that utilities should be able to recover prudently incurred, legitimate, and verifiable retail stranded costs arising from the transition to retail competition, if such costs cannot reasonably be mitigated. This federal policy should encourage States to provide for recovery of stranded costs because resolution of this issue is one of the key stumbling blocks that must be surmounted in order to provide choice to consumers. At the same time, the fundamental authority of States to address this difficult issue should be preserved. Recovery of investment in generating capacity has traditionally been overseen or regulated by State public utility commissions. In fact, thus far, all States that plan to implement retail competition have provided for utility stranded cost recovery in some manner. Under the Administration's proposal, States would continue to determine recovery of investments, including stranded cost recovery, under State law.

Nevertheless, to provide States with the ability to ensure that utilities within their borders can recover stranded costs, the Administration recommends that the Federal Energy Regulatory Commission be given the authority to provide a back-up mechanism for stranded cost recovery in particular instances where a State lacks authority to provide such recovery due to State constitutional constraints or other jurisdictional gaps. The United States government would not assume any stranded cost liability in the exercise by FERC of its backup authority on stranded costs.

II. PROTECTING CONSUMERS BY FACILITATING COMPETITIVE MARKETS

Encouraging States to implement competition is a necessary but not sufficient condition for the realization of competitive markets. Customers, who lack experience with competitive electricity markets, must have adequate information so they can get the lowest possible price on electricity. Moreover, eliminating monopoly franchises and cost-of-service regulation still leaves in place the traditional vertically-integrated utility structure that may not be suited for efficient and effective competitive markets.

A. Consumer Information

Proposal: *The Secretary of Energy would be authorized to conduct a rulemaking to require all suppliers of electricity to disclose information on price, terms, and conditions of their offerings; the type of generation source; and generation emissions characteristics.*

Under a retail monopoly structure, electricity consumers have no ability to choose suppliers, so there is generally no need for information comparing the price and environmental qualities of different electricity suppliers. In competitive markets, many different suppliers will offer a diverse menu of energy products and services with different pricing and billing options. Consequently, consumers will need reliable information so they can compare the products and prices offered by suppliers and make informed choices. To address this need, the Administration recommends that all electricity suppliers be required to disclose in a uniform, easy to read label, basic information on the price, terms and conditions of service sufficient to enable consumers to make comparisons among various offers.

Uniform and easy to understand labeling along the lines of the Food and Drug Administration's highly successful nutritional labeling system will ease customer choice. Research performed by the National Council on Competition and the Electric Industry showed that almost 60% of consumers they interviewed believed that they had enough information to make an informed choice when electricity products were uniformly labeled compared to 21% when no products were labeled. Both consumer and environmental groups have advocated an approach that would be modeled after the "nutrition facts" now on food. Details of such a labeling approach would be developed by DOE, with ample opportunity for public comment.

In addition, customers may wish to make their choice of supplier based on a consideration of environmental factors affected by their suppliers' generation mix. Customers interested in purchasing electricity produced using renewable resources, natural gas or other power sources will need assurances that representations as to general source and environmental characteristics are true. Participants in State pilot programs have frequently tried to differentiate their products by advertising them as "green." Some of their claims have been misleading, if not fraudulent. For example, in the New Hampshire pilot program, one supplier offered electricity which it claimed was generated by hydroelectric facilities. However, such power was, in fact, generated by pumped storage facilities. Another supplier claimed that the power it was selling was not generated by either nuclear or coal facilities. However, it was later learned that the power the supplier was selling as "green" power was in fact power generated, in part, from nuclear and coal facilities.

In addition to protecting consumers, a disclosure provision will also protect marketers that are selling truly "green" power, thereby encouraging greater participation by marketers in the "green" power market. For example, in California, six power marketers agreed to participate in the "Green-E" logo program, which requires each participant to market products that are based on at least 50 percent renewable-energy supply. Because use of the "Green-E" logo is limited only to participants in the program, such participants are given assurances that their fellow marketers of "green" power are satisfying the same minimum standards for "green" power sales.

A number of States considering the implementation of retail competition are also exploring the need for consumer disclosure requirements. In fact, the National Association of Regulatory Utility Commissioners passed a resolution in November 1996, supporting initiatives to require consumer disclosure. While the Administration encourages States to pursue such efforts, we nevertheless believe that, given the current movement toward regional markets, disclosure labels within and between regions must be uniform. Absent uniform disclosure labels, consumers may be unable to effectively compare products offered by many suppliers from many different parts of the country. Moreover, uniformity in disclosure requirements will better enable the relevant governmental agencies to verify the claims made by suppliers.

B. Public Utility Holding Company Act Repeal.

Proposal: *Repeal of substantive requirements of PUHCA. Provide FERC and State Commissions with additional access to the books and records of holding companies and affiliates of public utilities within holding companies to assist them in guarding against interaffiliate abuse following repeal of PUHCA, in combination with the other reforms, such as additional merger and market power authority.*

Congress enacted the Public Utility Holding Company Act ("PUHCA") in 1935 to break up the giant interstate utility holding companies that had formed and to preclude the recurrence of holding company financial abuses. However, many of PUHCA's requirements, such as the requirement that a holding company operate a single integrated utility system, are not compatible with a more competitive electricity market. Indeed, one of the objectives of competition is to encourage efficient builders and operators of generating capacity to participate in markets throughout the nation. Accordingly, the Administration supports the repeal of PUHCA as part of a comprehensive electricity restructuring bill.

Nevertheless, protection of consumer interests -- particularly guarding against cross-subsidization and abusive market power -- remains necessary. To assist in guarding against interaffiliate abuses that may disadvantage customers paying cost-of-service rates, FERC and State Commissions need greater access to the books and records of holding companies and the affiliates of public utilities within the holding companies, as well as additional authorities to address mergers and market power, which are discussed in the next two sections. The Administration would support enactment of S.621, by Senators D'Amato and Dodd, as part of comprehensive electric industry reform legislation.

C. Merger Review.

Proposal: *Establish FERC jurisdiction over the merger or consolidation of electricity utility holding companies and generation-only companies. FERC's review of mergers should be streamlined.*

A simple repeal of PUHCA would create a gap with regard to the regulation of mergers of public utility holding companies. Currently, FERC does not have clear jurisdiction over public utility holding company mergers or consolidations; such mergers are now subject to review by the SEC under PUHCA. Accordingly, section 203 of the Federal Power Act should be modified to provide FERC with jurisdiction over the merger of public utility holding companies. In addition, FERC does not have jurisdiction over generation facilities. In a largely deregulated generation market, mergers of generation-only utilities could result in market power in the generation market, and the FPA should therefore be amended to provide FERC with jurisdiction over the merger of these entities. Finally, to further streamline the Commission's review process, section 203 of the FPA should be amended to clarify that an on-the-record hearing is not required for each merger application.

D. Authority to Address Market Power

Proposal: *Authorize FERC to remedy wholesale market power if FERC finds market power in wholesale markets. Authorize FERC, upon petition from a State, to remedy market power in retail markets if the State is implementing retail competition, finds market power, and has insufficient authority to remedy the market power. FERC would be authorized in these circumstances to require generators with market power*

to submit a plan to mitigate market power, which FERC could approve with or without modification. FERC would be authorized to order divestiture to the extent necessary to mitigate market power.

The Commission's recently issued rules requiring open and comparable access to transmission services and information (Order Nos. 888 and 889) should, when fully implemented, largely mitigate market power associated with the control of transmission facilities. However, open transmission access will not, by itself, prevent the exercise all forms of market power in electricity markets. A utility can possess market power simply as the result of its ownership of all or substantially all of the generation facilities within a market. However, the mere presence of market power would not trigger application of the antitrust prohibitions. In addition, physical transmission constraints could limit the geographic scope of markets especially during certain seasons or time periods.

FERC currently has the authority to condition merger applications to remedy any potential market power. Absent a merger application, FERC's only other available tool to address market power is to deny a request for market-based rates. However, such action would severely impede the Commission's ability to promote wholesale competition. To ensure that the development of competition is not hindered by the exercise of market power, the FPA should be amended to give the Commission the authority to remedy concentrations of market power in the wholesale market, including the authority to order the divestiture of assets, if such market power is found.

Under the Administration's approach, States retain the primary responsibility for implementing retail competition. In opening their markets to competition, States are likely to address market power problems. However, because of the regional nature of many markets, a State may be presented with a market power problem that extends beyond its borders and its jurisdiction. Accordingly, the Administration recommends that FERC be authorized to provide "backup" market power remedies, including divestiture of assets, if a State is implementing retail competition, finds that one or more suppliers have market power in those retail markets, has insufficient authority to remedy the market power itself, and asks FERC to take action. Given that a requirement to divest assets is an extraordinary remedy, FERC should in the first instance consider proposals by the generators possessing market power on how to mitigate market power through less intrusive means. FERC would be authorized to order divestiture only to the extent necessary to mitigate market power.

III. ASSURING ACCESS TO AND RELIABILITY OF THE TRANSMISSION SYSTEM

To realize a fully competitive market, transmission must be available on a non-discriminatory basis, must be reliable, and must be adequate to accommodate the many and required transactions. In a regulated market, the regulated utilities worked in tandem with their regulators and neighboring utilities to ensure that the transmission system was adequate and secure. However, a competitive market will require a different approach.

A. Strengthen Electric System Reliability

Proposal: *The Federal Power Act should be amended to require FERC to approve the formation of and oversee a private self-regulatory organization that prescribes and enforces mandatory reliability standards.*

The electric utility industry, through a tradition of voluntary self-regulation and cooperation, has performed admirably in maintaining reliability over the past thirty years. However, in a highly competitive market environment, a different mix of incentives will be at work. There will be pressures to cut costs and to drive the power grids harder, to squeeze as much economic value out of them as possible without causing a system breakdown. Moreover, since many transmission owners will also be in the power generation and marketing business, there may also be an incentive to exercise control over strategic parts of the transmission system for economic purposes, perhaps using reliability concerns as a pretext.

As a result, we need to establish through federal legislation a framework that will build upon and maintain the industry's tradition of self regulation, but require all participants in physical electric transactions on the grid to comply with mandatory reliability standards. The FPA should be amended to give FERC the authority to approve and oversee a self-regulating organization that will prescribe and enforce mandatory electric reliability standards. Federal oversight is required to provide legal support for a private self-regulating structure. Under this approach, FERC will be given the authority to review all mandatory reliability standards developed by the self-regulating organization to ensure that they are in the public interest and reflect an appropriate level of reliability. FERC's review of such standards will also give recognition to the technical expertise of the self-regulating organization. Membership in the self-regulating system will be open to all entities that use the bulk-power system and should be required for all entities whose behavior is critical to system reliability. Under the oversight of FERC, the private self-regulating organization system will monitor compliance with the reliability standards and, when necessary, enforce compliance with the standards.

The Department of Energy's Task Force on Electric System Reliability, an independent advisory body chaired by Dr. Philip Sharp, the former Chair of the U.S. House of Representatives Energy and Power Subcommittee, has submitted findings and recommendations to DOE regarding an appropriate reliability framework. These recommendations serve as the foundation for our proposal.

B. Authority to Establish and Require Independent System Operation

Proposal: *Amend the FPA to provide FERC with the authority to require transmitting utilities to turn over operational control of transmission facilities to an independent system operator.*

As a result of Order No. 888, all public utilities are required to provide open and non-discriminatory access to transmission facilities for wholesale buyers and sellers. This rule is intended to reduce a transmission owner or operator's ability to discriminate in the provision of transmission services. However, separation of the operation and control of transmission facilities from generation through participation in an independent system operator (ISO) structure would greatly reduce the risk that operation of the transmission system could be distorted to favor some generators or customers over others.

The benefits of the independent operation of the transmission system are clear. A network of regional-scale ISOs addresses concerns about the exercise of market power by transmission owners. An efficiently dispatched and properly priced bulk power system might not develop absent the establishment of regional independent system operators. Yet, the unwillingness of some transmission operators to join an ISO could prevent the successful formation of such entities.

FERC's authority to require an investor-owned utility to join an ISO is not clear, and it appears to have no authority to require either public power or cooperative entities to join an ISO. We propose that FERC be given the authority to require that any transmission owner, regardless of its ownership structure or FERC's jurisdiction over other aspects of its operations, participate in an ISO, and to set other requirements pertaining to ISOs as needed to serve the public interest.

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C. Regional Transmission Planning Agencies

Proposal: *Amend federal law to encourage the development of regional transmission planning and siting groups.*

The electric utility industry is moving toward regional markets. The recent proposals for regional Independent System Operators recognize the importance of aiding regional markets to achieve greater economic and system efficiency. However, an effective and efficient regional market requires the effective planning and siting of new generation, transmission and distribution facilities. A regional transmission planning agency would best respond to the needs of an evolving regional market.

An interstate compact would be necessary to pursue regional planning and siting, and such a compact must be approved by Congress. The Administration supports legislation which would provide the required Congressional consent for compacts which FERC finds meet the specified criteria relating to the workability of the structure, that is, each participating State has given the regional agency a uniform grant of authority and decisionmaking rules do not involve supermajority requirements that could stalemate the body. This authority to approve regional planning bodies would supplement, not replace, the current joint board authority found in section 209 of the FPA.

IV. PROMOTING AND PRESERVING PUBLIC BENEFITS

Existing programs providing support for renewable energy and other important public benefits were designed for a system of regulated markets. These programs require modification to continue their important contribution towards meeting environmental and economic policy goals within the context of a competitive market. The Administration's proposal on restructuring includes provisions that promote the continued pursuit of public interest goals, including improving air quality, within the framework of competitive markets.

A. Secure The Future of Renewable Electricity Through a Renewable Portfolio Standard

Proposal: *Adopt a federal Renewable Portfolio Standard (RPS) to guarantee that a minimum level of additional renewable generation is developed in the United States. The RPS would require electricity sellers to cover a percentage of their electricity sales with generation from non-hydroelectric renewable technologies such as wind, solar, biomass or geothermal generation. The RPS requirement would be initially set close to the ratio of RPS-eligible generation to retail electricity sales projected under baseline conditions. There would be an intermediate increase in RPS requirement in 2005, followed by an increase to 5.5% in 2010.* The RPS should be subject to a cost cap.

Repeal prospectively the "must buy" provision of section 210 of the Public Utility Regulatory Policies Act (PURPA), but preserve existing contracts and exemptions.

Retail competition itself has the potential to significantly increase renewable energy's share of the electricity market, because it will allow environmentally-conscious consumers to support green energy technologies with their wallets. Nonetheless, the inherent uncertainty of the transition to competition, the recognition of important environmental and energy diversification benefits from renewables, and the fact that existing PURPA requirements and State initiatives to promote renewable energy are both incompatible with competition and ineffective under present market conditions all suggest that federal policy towards renewable electricity should be revisited in the context of restructuring. To this end, the Administration supports a federal Renewable Portfolio Standard that would require all electricity sellers to cover a percentage of their electricity sales with generation from non-hydroelectric renewable sources such as wind, solar, biomass or geothermal energy.

Retail sellers could meet the proposed RPS requirement by generating sufficient renewable electricity to meet the coverage ratio, by purchasing tradeable renewable electricity credits (RECs) that would be created and tracked for each unit of RPS-eligible renewable electricity produced, or by some combination of these strategies. In contrast to the facility-based requirement of PURPA, our proposed definition of eligible renewable generation focuses directly on the use of renewable fuels or sources. All generation using RPS-eligible renewable fuels or sources could receive RECs, regardless of whether the fuels are used in new or existing facilities or whether the electricity generated from eligible renewable sources is sold on the grid. Where RPS-eligible and non-RPS eligible fuels are used in the same facility, RECs would be awarded based on the proportion of RPS-eligible renewable fuel multiplied by total generation. However, sources that elect the kind of net metering discussed in a later section of this Plan could not also receive RECs.

The Administration proposes that the RPS requirement be initially set close to the ratio of RPS-eligible generation to retail electricity sales projected under baseline conditions. There would be an intermediate increase in the RPS requirement in 2005, followed by an increase to 5.5% in 2010. The RPS would expire in 2015, when the economics and benefits of renewable technologies are expected to be firmly established. The RPS would include a provision for banking of RECs, to encourage a smooth and continuous ramp-up of renewable electricity production during the interval between RPS adjustment points. In addition, our proposal provides for a backup cost cap to hold program costs below a pre-specified ceiling. The market-based approach of the RPS mechanisms and the cost cap will assure that we maintain a reasonable balance between the costs of the RPS program and its environmental and energy independence benefits, and will strongly encourage efforts to reduce the costs of renewable electricity generation technologies.

PURPA, enacted in 1978, fostered the commercialization of renewable energy through section 210's requirement that a utility purchase power from cogenerators and renewable energy facilities (QFs) at the utility's avoided cost. Section 210 has had the incidental benefit of introducing competitive procurement practices in the electric utility industry. However, in competitive markets, the market access protections for qualifying facilities (QFs) provided by Section 210 of PURPA are no longer needed to ensure fair opportunities for non-utility power producers. Moreover, it is unreasonable to apply a "must buy" requirement to electric utilities in a competitive market, where they have no captive customers required to pay a premium for QF power. Further, under present market conditions, PURPA is not an effective mechanism to support renewable energy technologies.

The RPS employs market forces through renewable energy credit trading, and spreads the cost of supporting renewable generation more evenly across the retail electricity market than does PURPA's "must buy" provision. It also avoids the need for troublesome regulatory determinations regarding "avoided cost." We therefore propose to repeal the "must buy" provision

of section 210 of PURPA prospectively in favor of a more flexible and economically efficient renewable portfolio standard. However, the amendments to PURPA should clarify that existing contracts would not be affected by any prospective change in the obligation to purchase under section 210. Moreover, the regulatory exemptions under applicable federal and State law for existing QFs should also be preserved together with their right to interconnection, backup and standby power on reasonable terms.

It should be noted that other elements of the Administration proposal will also encourage the development of renewable electricity generation. These include consumer disclosure requirements, which should further help the development of renewable energy, and a net metering provision that is likely to be of particular benefit to small scale solar generation technologies. In addition, States may provide additional support to renewable technologies through the public benefit fund.

. B. Encourage and Support Continued Funding for Public Benefit Programs

Proposal: *Create a $3 billion per year public benefit fund to provide matching funds to States for low-income assistance, energy efficiency programs, consumer education and the development and demonstration of emerging technologies, particularly renewables.*

The Administration supports the creation of a $3 billion per year public benefit fund (PBF) to provide matching funds to States for low-income assistance, energy efficiency programs, consumer education and the development and demonstration of emerging technologies, particularly renewables. The PBF would be funded through a generation or transmission interconnection fee on all electricity, capped at 1/10 of one cent (1 mill) per kilowatt-hour. It would be overseen by a Joint Board composed of Federal and State officials who would set standards for fund eligibility. States would have the flexibility to decide whether to seek funds and how to allocate funds among public purposes. Within each State, programs such as renewable development and energy efficiency should compete for funds on the basis of cost-effectiveness. The PBF will sunset after 15 years of operation.

The introduction of competition itself should provide important public benefits, as sellers will have a strong incentive to add value to and differentiate their products in ways that will provide such benefits. Initial experience with pilot programs and nascent competition suggest that, as strategies to attract and retain customers, companies will provide bundled packages of electricity and efficiency services (instead of a “raw electricity” commodity) and sell renewable (“green”) power as a premium product to environmentally-conscious consumers.

Nevertheless, if not properly implemented, retail competition could lead to reduced support for electricity-related programs that provide important public benefits. Under cost-of-service regulation, programs supporting and promoting renewable generation, energy efficiency and low-income assistance were supported in part through utility rate structures, and utilities recovered the costs of approved programs within their monopoly service area as a part of the overall cost of service. As utilities prepare for competition, such entities will be unwilling to include in their rates the cost of programs not included in the rates of their competitors. Moreover, although transmission and distribution will remain regulated, public benefits programs will suffer if States do not continue to require funding for these programs.

A number of States that plan to open their electricity markets to retail competition are already planning to recover the costs of certain public benefit programs through a non-bypassable distribution charge on all electricity customers. A federal PBF will both encourage and support the

creation of these programs at the State level, and can be structured to give States the flexibility to allocate public benefit funding in a manner that addresses unique State or local needs. A federal PBF is also justified by the fact that many of the activities in question provide public benefits that transcend State boundaries. Finally, the proposed matching fund amount of $3 billion will encourage States, at a minimum, to preserve the current level of support States provide for public purpose programs, estimated at about $6 billion in 1996.

Lower-cost renewable technologies such as wind, geothermal and biomass, which receive considerable support through current utility rates, would be supported primarily through the Renewable Portfolio Standard. No "double dipping" would be permitted for renewable projects. Such projects could only receive support from either the RPS or the PBF, but in no instance could receive support from both mechanisms.

C. Net Metering

Proposal: *Make all consumers eligible for net metering and require that all distribution service providers assure the availability of interconnection, subject to appropriate nondiscriminatory safety standards. The provision should apply only to very small (up to 20 kW) renewable energy projects, and be subject to a cap determined at the state level.*

Net metering provides an incentive for electricity users to install small-scale on-site renewable generation sources (such as the rooftop solar photovoltaic panels featured in the President's *Million Solar Roofs Initiative* announced in June, 1997) in order to reduce electricity generation from conventional sources. The net metering customer maintains the benefit of connection to the power network, but saves on both transmission and distribution charges and power charges when renewable energy is being generated either for use or for resale to the grid.

A federal requirement to provide net metering arrangements would provide support for dispersed, small, renewable generation resources. Accordingly, the Administration recommends that all consumers be made eligible for net metering. The provision should also require that all distribution service providers assure the availability of interconnection, subject to appropriate nondiscriminatory safety standards. Such non-discriminatory interconnection standards would apply to all reasonable interconnection requests. Finally, the provision should apply only to very small (up to 20 kW) renewable energy projects.

D. Nitrogen Oxide Trading Authority

Proposal: *Clarify EPA authority to require a cost-effective interstate trading system for nitrogen oxide (N0x) pollutant reductions addressing the regional transport contributions needed to attain and maintain the Primary National Ambient Air Quality Standards (PNAAQS) for ozone. No change is proposed to existing EPA authority to determine geographic coverage or level of reductions required in addressing regional transport contributions.*

Our restructuring proposal is likely to provide net benefits to the environment by reducing emissions of nitrogen oxides (N0x) and carbon dioxide relative to baseline projections for 2010. Notwithstanding these benefits, the work of the Ozone Transport Assessment Group (OTAG), a multi-year consultative process that included representatives from states, public interest groups, and electric utilities throughout the Eastern United States, suggested that a further substantial reduction in NOx emissions over a wide area is needed to attain the ambient health-based standard

for ozone in the Northeast. Electric generators are a major source of NOx emissions.

In November 1997, the Environmental Protection Agency (EPA) proposed to address the regional transport of NO_X emissions that contribute to violations of the Primary Ambient Air Quality Standard for Ozone through a set of NO_X emissions budgets to apply to 22 eastern States and the District of Columbia under authority provided in Section 110 of the Clean Air Act. EPA's proposal is based on the work of OTAG.

Both air quality and economic interests favor the use of efficient market-based instruments to achieve the emissions reductions necessary to address adverse regional transport impacts. To this end, EPA has proposed to allow interstate trading of budgeted emissions allowances. However, States may be reluctant to take advantage of this flexibility. The Administration therefore proposes to clarify EPA's authority to require a cap and trade system for nitrogen oxides.

Our proposal would not affect either the level of emissions reductions, or the geographic area over which reductions should be made, to address regional transport of emissions. The ongoing regulatory processes under existing statutory authority are the appropriate venue for addressing these technical issues.

E. Air Emissions

The Administration believes that retail competition will deliver economic savings, cleaner air and a down-payment on greenhouse gas emissions reductions. We estimate that our Competition Plan will reduce greenhouse gas emissions by 25 to 40 million metric tons by the year 2010.

As previously discussed, our plan includes a Public Benefits Fund of up to $3 billion annually (1.0 mill/kWh,) to match State commitments for financing energy efficiency, renewable energy, and other public benefit programs; "green labeling" provisions to help consumers identify and choose power from environmentally friendly generators; a Renewable Portfolio Standard, to require that at least 5.5 percent of electricity sales be generated from non-hydroelectric renewable sources, subject to a cost cap; a net metering provision encouraging the installation of small renewable systems; and trading authority NO_X for emissions, to facilitate cost-effective, market-driven NO_X reductions. In addition, we expect that retail competition will strengthen incentives to improve efficiency, and reduce the two-thirds waste of energy currently associated with fossil-fuel generation of electricity -- thereby further cutting greenhouse gas emissions, saving money, reducing pollution, and conserving fuel.

We believe that our plan will produce cleaner air and reduced greenhouse gas reductions, although the precise impacts are difficult to predict. We intend to work with the Congress to ensure that any unanticipated consequences are addressed quickly and in keeping with the Administration's climate change policies.

Therefore, those making investment decisions through the period of restructuring should recognize the Administration's strong commitment to reducing greenhouse gas emissions on the timetable set out in the President's climate change policy. We are not asking this Congress for carbon cap-and-trade authority as part of the Administration's electricity restructuring proposal. The Administration's climate change policy calls for cap-and-trade authority to be in place by 2008, and the Administration will consider in consultation with Congress whatever legislative vehicle is most appropriate for this purpose.

In the meanwhile, the Administration will seek to ensure that we have accurate, accessible data on the progress toward cleaner air and carbon dioxide reduction. Under current law, the utility industry reports various types of emissions. The Administration intends to ensure that the relevant Federal agencies coordinate the data received on emissions from the utility sector and then provide such data in annual reports to the President.

F. Rural Safety Net

The Administration is confident that a properly structured retail competition system will benefit consumers in all parts of the nation, including rural areas. Nevertheless, the Administration is mindful of the possibility that in certain cases competition could have adverse impacts in rural areas where the cost of delivering electricity to consumers is relatively high. Accordingly, a rural safety net should, if necessary, be established to address any unintended consequences arising from the transition to retail competition. DOE and USDA staff are currently working together on analysis to determine the likely impact of competition on rural areas.

V. AMENDING EXISTING FEDERAL STATUTES TO CLARIFY FEDERAL AND STATE AUTHORITY

The existing Federal regulatory framework for the electric power industry was established early in the New Deal with the enactment of the Federal Power Act and the Public Utility Holding Company Act. The State regulatory structure, for the most part, preceded these federal statutes. This regulatory framework has remained essentially unchanged: vertically-integrated utilities enjoy the advantages of monopoly franchise territories and authorized rates of return on investment, in exchange for an obligation to serve all customers within their respective service territories at regulated rates.

The federal statutory framework does not readily accommodate individual State initiatives to institute competition among retail suppliers. In fact, certain federal statutes which were drafted in the context of cost-of-service regulation may prove unworkable in a restructured market. Moreover, FERC may be unable to fully implement its open-access policy absent increased authority under the Federal Power Act. Amendments to the Federal Power Act will be necessary in order to enable both FERC and the States to implement competition effectively.

A. Clarify Federal Jurisdiction

Proposal: *Provide FERC with clear authority to order retail transmission in a transmission system other than where the end user is located to complete an authorized retail sale.*

Reinforce FERC jurisdiction over rates, terms, and conditions of unbundled retail transmission.

Reinforce FERC authority relied upon to promulgate Order No. 888.

Provide that FERC's open access rules apply to municipal utilities, cooperatives, the Tennessee Valley Authority (TVA), and Federal power marketing administrations (PMAs), with the proviso that, with respect to the PMAs, TVA, and cooperatives financed by the Rural Utilities Service, it may be necessary in some instances to adopt special stranded cost mechanisms to take into account the unique facts and circumstances surrounding these federal investments or loans.

A number of technical changes to the Federal Power Act (FPA) are needed to ensure that the jurisdiction of the Federal Energy Regulatory Commission (FERC) is sufficient to protect consumers in the newly competitive framework in electricity markets. First, FERC should have clear authority to order transmitting utilities to provide retail transmission in a utility system other than where the end user is located if needed to complete a State-authorized retail sale. This clarification of the law is necessary to ensure that transmission system owners in one system do not have the ability to frustrate State-sanctioned retail sales in another system. In addition, FERC's jurisdiction over rates, terms, and conditions for unbundled retail transmission should be clarified to avoid the potential burden of duplicative and potentially conflicting regulation in this area by providing FERC with jurisdiction over such transmission.

In 1996, FERC issued its landmark orders (Order Nos. 888 and 889) requiring jurisdictional utilities to file open access transmission tariffs. This was a critical step in opening markets to competition. However, FERC's authorities to require the filing of open access tariffs and to allow for the recovery of stranded costs resulting from the implementation of open access have been challenged. To ensure that open access will be implemented without any cloud of legal uncertainty, the FPA should be amended to remove any doubt that FERC has the authority to require the filing of open access tariffs by rule without a hearing and that FERC has the authority to allow utilities to recover stranded costs resulting from implementation of the open transmission access requirement.

Order No. 888 applies to public utilities, but it does not apply directly to entities such as the Federal power marketing administrations (PMAs), rural electric cooperatives, and municipalities. Effective wholesale competition requires that suppliers and purchasers of electricity have comparable access to all necessary transmission facilities. Limiting open access tariff requirements to those utilities subject to the Commission's ratemaking jurisdiction would constrain and distort the development of competitive power markets. Accordingly, to provide for greater and more efficient competition, the transmission rates, terms and conditions of non-jurisdictional utilities should be subject to the Commission's jurisdiction and open access rules.

While the Administration supports the mandatory application of the Commission's open access requirements to non-jurisdictional utilities, with regard to the PMAs, the Tennessee Valley Authority (TVA), and rural electric cooperatives financed in part by the Department of Agriculture Rural Utility Service (RUS), the Administration supports such application with the proviso that it may be necessary in some instances to adopt special stranded cost authorities that take into account the unique facts and circumstances surrounding these federal investments or loans. This is an important issue because the combined debt of RUS, TVA, and the Bonneville Power Administration (BPA) is over $70 billion. One possible approach is to authorize the Commission to suspend or modify the application of open access requirements to these entities for specified periods if it finds that adequate stranded cost mechanisms are not in place (see also discussion below regarding role of Federal power agencies).

We are pleased to note that the PMAs are acting voluntarily to comply with FERC open access requirements. The Bonneville Power Administration's (BPA) open access transmission tariff has been conditionally approved by the Commission and the other PMAs that own transmission, the Western Area and Southwestern Power Administrations, filed open access tariffs in December 1997 for review and approval by the Commission.

B. Clarify State Jurisdiction to Implement Retail Competition

Proposal *Amend the Federal Power Act (FPA) to clarify that it does not preempt States from ordering retail competition.*

Amend the FPA to clarify that it does not preempt States from imposing a charge on the ultimate consumers receipt of electric energy.

The FPA should be amended to clarify that it does not preempt States from ordering retail competition. At least two State retail competition plans have been challenged on these grounds, and other such challenges are likely if this matter is not addressed. The FPA should also be amended to clarify that it does not preempt States from imposing a charge on the ultimate customer's receipt of electric energy. Such charges are being used by States to allow for the recovery of stranded costs and to fund public benefits programs.

C. Clarify State Authority to Impose Reciprocity Requirements

Proposal: *Provide States that have implemented retail competition with the authority to preclude an out-of-state utility with a retail monopoly from selling within the State unless that out-of-state utility permits customer choice.*

Retail competition will enable currently captive retail customers to purchase power from alternative suppliers. Such competition will likely result in some utilities losing a portion of their existing load to outside suppliers. If neighboring utilities allow retail competition, the utility with surplus power due to the advent of retail competition in its own formerly exclusive service area could mitigate or eliminate stranded costs by selling its surplus to the customers of these utilities. However, if neighboring utilities are not subject to a retail competition requirement, a utility in this situation would have greater difficulty in mitigating its losses and the amount of its stranded costs would likely increase.

States can assist utilities in gaining access to the customers of utilities over which the State has no ratemaking authority ("extra-jurisdictional utilities") by imposing a reciprocity requirement. Such a requirement would condition an extra-jurisdictional utility's access to customers of the jurisdictional utility on the extra-jurisdictional utility's providing retail access to its own customers. However, some States have expressed concern that the Commerce Clause would limit their ability to impose reciprocity requirements on extra-jurisdictional suppliers. To provide States with clear authority, the Federal Power Act should be amended to provide States with the authority to impose a reciprocity requirement on all extra-jurisdictional suppliers of electricity within the United States.

A Commerce Clause challenge could also be raised with respect to a State's attempt to prevent low-cost indigenous power from being sold to customers outside the State following implementation of retail competition, which could have the effect of increasing electricity rates for in-State consumers. We are considering whether States should be given specific authority to preserve such low-cost indigenous power following implementation of retail competition.

D. The Appropriate Role of Federal Power Agencies

The Administration is also considering the question of the appropriate role of the federal power agencies, particularly BPA and the Tennessee Valley Authority (TVA), in the new competitive market. The Administration is favorably inclined toward the recommendations made concerning BPA by the Comprehensive Review of the Northwest Energy System, a public stakeholder

process sponsored by the Governors of Washington, Oregon, Idaho and Montana. However, issues such as stranded costs, which were not adequately addressed by the Review, must be resolved before we have a complete blueprint for adapting BPA to competition. Appropriate resolution of this matter is critical to assuring that the costs and liabilities associated with Bonneville, including Federal and Washington Public Power Supply System debt, continue to be borne by the beneficiaries of the Bonneville system, not Federal taxpayers. The Northwest Governors Transition Board is addressing the stranded cost issue, and we look forward to receiving its recommendations.

The Administration is also considering the issue of the introduction of both wholesale and retail competition to the TVA service area. As a first step, we have established the independent Tennessee Valley Electric System Advisory Committee, under the authority of the Secretary of Energy Advisory Board, and chaired by former Congressman Butler Derrick. The Committee is comprised of a broad spectrum of TVA stakeholder and is working together to develop recommendations for restructuring the power activities of TVA. We expect them to provide us with a broad framework for bringing competition to TVA and restructuring its operations. We look forward to the committee's recommendations, which it intends to produce by March 31, 1998.

VI. MISCELLANEOUS PROVISIONS

A. Amendment to Bankruptcy Reform Act

Proposal: *Amend the Bankruptcy Act to make nuclear decommissioning costs a nondischargeable priority claim.*

Nuclear decommissioning costs should be a nondischargeable priority claim in a bankruptcy proceeding, which would ensure that no licensee would be able to avoid decommissioning liability. Section 503(b) of the Bankruptcy Reform Act of 1978 should be amended to provide that such costs should be a nondischargeable priority claim.

B. EIA Study of Impacts of Competition

Proposal: *The Energy Information Administration should be directed to study the impacts of wholesale and retail competition.*

The collection of information relating to the impacts of wholesale and retail competition will be critical to the Federal and State governments' respective examinations of whether customers are receiving the economic benefits of an efficient competitive market, to suppliers' efforts to operate and plan efficiently, and to consumers' decisions as to which supplier of electricity best meets their needs. Provisions which would more thoroughly specify the information authorized to be collected by the Administrator for a study on the impacts of competition would enable the Energy Information Administration to justify collection of this information, especially to reluctant information providers. Accordingly, the Administration recommends legislation to direct such an EIA study, and to authorize EIA to collect the necessary information.

C. Effect on operation of antitrust laws

Proposal: *Provide that nothing in the new legislation affects operation of antitrust laws.*

Continued and effective operation of the antitrust laws is of critical importance in the successful implementation of retail competition. Accordingly, the Administration recommends the inclusion of an antitrust savings clause which provides that nothing in the legislation would be construed to modify, impair, or supersede the operation of the antitrust laws.

D. Eliminate antitrust review by Nuclear Regulatory Commission

Proposal: Eliminate antitrust review by NRC.

Section 105c of the Atomic Energy Act (AEA) requires antitrust reviews by the Nuclear Regulatory Commission in connection with applications for an NRC license to construct or operate a commercial utilization or production facility. However, such reviews are no longer necessary in light of the authority of the Justice Department and the Federal Energy Regulatory Commission with respect to utility market power issues. Thus, the Administration recommends that section 105c be stricken from the Atomic Energy Act. This amendment to the AEA would nevertheless leave intact existing antitrust license conditions and the NRC's authority to enforce those existing conditions.

E. Taxes

(1) Nuclear Decommissioning Costs

Proposal: Amend the Internal Revenue Code relating to deductions to a qualified nuclear decommissioning fund.

The amount of contributions to a qualified nuclear decommissioning fund a utility is entitled to deduct under section 468A of the Internal Revenue Code is the lesser of the "cost-of-service" amount or the "ruling amount." In a restructured market, if a nuclear power plant is no longer subject to cost-of-service ratemaking, it could be determined that the amount of decommissioning costs included in cost-of-service would be zero. Because the amount qualified for the tax deduction is the lesser of the amount included in the cost of service or the ruling amount, the tax deduction would then be zero. To address this problem, section 468A needs to be amended.

(2) Tax-Exempt Bonds

Proposal: Amend the Internal Revenue Code to provide that (1) private use limitations are inapplicable to outstanding bonds for publicly-owned generation, transmission or distribution facilities if used in connection with retail competition or open access transmission, and (2) tax-exempt financing is unavailable for new generation or transmission facilities. Tax-exempt financing would continue to be available for distribution facilities subject to current law private use limitations.

Restructuring of the electric utility industry forces a reexamination of the rules governing the use of tax-exempt bonds to finance facilities for the generation, transmission and distribution of electricity. The basic framework of current law rules was established to fit an era when individual electric systems, whether privately or publicly-owned, operated within clearly defined service territories and when the wheeling of power was not widely practiced. The basic premise of these rules is that tax-exempt bond financing is not generally available for facilities used to a significant extent by private persons in a capacity other than as a member of the general public. As the industry moves toward a more efficient, integrated structure, transmission and distribution facilities

financed in prior years with tax-exempt bonds need to be open to use by private firms in the business of generating electricity. Public power systems are expected to participate in restructured environments that allow competing, private generators of electricity to sell to customers who formerly had no option but to be supplied by those public systems.

The efficiency and equity of a restructured industry depends upon leveling the playing field with respect to capital costs while at the same time ensuring that publicly-owned facilities are not discouraged by the federal income tax rules from fully participating.

Accordingly, the Administration recommends that facilities financed with outstanding tax-exempt bonds should be free from the private use limitations provided that (i) such facilities continue to be owned by public entities, and (ii) such generation, transmission and distribution facilities are used in connection with retail competition or open access transmission. The Administration further recommends that new generation and transmission facilities be ineligible for tax-exempt bond financing. The Administration recognizes that certain situations may warrant transition or other relief and would like to work with Congress to identify such situations and develop appropriate relief measures. Tax-exempt financing would continue to be available for distribution facilities subject to current law private use limitations.